



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE

WASHINGTON, D.C. 20224

NO PROCEEDINGS RECEIVED  
Release to Manager, NO Determinations - Cincinnati

Date: FEB 16 2001

DATE: [REDACTED]

SURNAME [REDACTED]

Contact Person: [REDACTED]

ID Number: [REDACTED]

Contact Number: [REDACTED]

[REDACTED]

Employer Identification Number: [REDACTED]

Dear Applicant:

This is in reply to your application for recognition of exemption under section 501(c)(3) of the Internal Revenue Code.

We have considered the information you have submitted and have concluded that you have not established that you qualify for recognition of exemption under section 501(c)(3) of the Code. The information you have submitted establishes that many of your proposed activities are not yet operational and that the infrastructure needed by the [REDACTED] to enable you to carry on your program is not present. Furthermore, you currently appear to operate in a manner which benefits [REDACTED] to more than an insubstantial degree.

You were established for educational purposes. You have represented that your resources will be devoted exclusively to establishing a system for interactive teleconferencing between dentists located in the lower [REDACTED] and the diagnostic and clinical departments of the [REDACTED]. You also state that you will serve as a remote site for doctors and dentists to attend and receive credit for continuing education programs and also serve as an alternate remote site for attending transmitted lectures as part of a degree or certification program. You also expect to establish an informational web site. Funding for the purchase of the computers and other equipment and programs needed to accomplish these goals was provided by a loan from a commercial source. You describe the area you are located in and shall be serving as a historically recognized medically underserved area. The information you have submitted establishes that your program is still in its infancy.

You state that you have provided or assisted in providing approximately three to four continuing education courses each year over the last two years. The program announcements you provided indicate that these programs have run from one to seven hours and have been put on in conjunction with other organizations. You have indicated that the total number of hours you spent per year on all your educational programs totaled approximately [REDACTED] hours and the costs incurred per year on this aspect of your program were \$[REDACTED] per year. It does not appear that you have engaged in any of the other

activities you propose to do. You have not advertised your facilities as being available to the dental community to set up teleconferences for medical assistance in particular patient cases. You have not established a dental oriented web site for the public nor do you have your own sites for putting on continuing education programs. Finally you have not acted as a site for attending lecturers to hold teleconferences. In addition, you have represented that the entire videoconferencing program of the [REDACTED] is still in the development al stage.

You state that half of the officers on your board of directors are also principal shareholders in, [REDACTED], a for profit dental practice (hereinafter referred to as [REDACTED]). The remaining two directors also appear to have a business relationship with [REDACTED]. You share space with [REDACTED] in at least two sites and the dental practice is leasing your computer and telecommunication equipment from you to treat and bill its own dental patients. It appears that you purchased or otherwise obtained the programs [REDACTED] uses for its office management, even though such programs have little or no connection to the accomplishment of your exempt purposes. It also appears that you are currently seeking a grant to extend your program to [REDACTED] third business office. This latest grant request again includes a request for business software, which you indicate in your letter of [REDACTED] is only need by [REDACTED] to carry on its practice. You represent that [REDACTED] utilizes approximately 90 percent of your communication equipment, telephone lines and network equipment. However, you expect your use to grow as you become better known in the community. You also indicate that at any given time at least 3 of your 12 available workstations are not in use by [REDACTED] and that you can utilize your equipment contemporaneously with [REDACTED] without any interference between with either your educational activities or their business activities.

The lease with [REDACTED] is renewable and set for a five year term. This lease includes the equipment located at each of the business sites of [REDACTED]. However, it does not appear that one of their business offices has any videoconferencing capabilities yet. You have represented that the lease rate was determined after evaluating your fixed and variable costs for the equipment and telecommunication lines. This also includes maintenance costs and other recurring costs. You have represent that you consider your fees to be competitive with local market rates. However, you state that you were unable to obtain price quotations from other entities for providing same type of telecommunications services and equipment. On the other hand, you were able to obtain a letter from a certified public accountant who upon consideration of the detailed listing of equipment associated with the lease and the note agreement associated with the equipment financing concluded that "the lease payment is a fair market lease rate for the computer and videoconferencing equipment associated with this lease". The lease agreement calls for the payment of \$[REDACTED] monthly and your required monthly loan payment is \$[REDACTED]. The two board members who are also principals of [REDACTED] participated in decisions concerning the lease arrangements and fees involved. Furthermore, we note that the other two directors have a business relationship with [REDACTED].

Income from this lease is your primary continuous source of funding. [REDACTED] has also provided you use of its facilities and occasional use of its employees without cost. Other smaller sources of income are fees to participate in continuing education programs. Here again you have represented that the fees charged to attend continuing professional education programs are set at the minimum fee possible that will allow you to recover the costs incurred in presenting the programs and allow for planning of future programs

Section 501(c)(3) of the Code describes organizations organized and operated exclusively for religious, charitable and educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations states that in order to be exempt as an organization described in section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more purposes specified in that section. If an organization does not meet either the organizational or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more of the purposes specified in section 501(c)(3) unless it serves a public rather than a private interest. Thus, to meet these requirements, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" is used in section 501(c)(3) in its generally accepted legal sense. It includes relief of the poor and distressed, the advancement of religion, the advancement of education and lessening the burdens of government.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), Ct.D. 1650, C.B. 1945, 375, the Supreme Court of the United States held that the presence of a nonexempt purpose, if more than insubstantial, would destroy tax exempt status as a charitable organization.

In United States v. Wells Fargo Bank, 485 U.S. 351, 108 S. Ct. 1179, 99 L.Ed. 2d 368 (1988), the Supreme Court held that an organization must prove unambiguously that it qualifies for a tax exemption.

Harding Hospital, Inc. v. United States, 505 F.2d 1068 (1974), holds that an organization seeking a ruling as to recognition of its tax exempt status has the burden of proving that it satisfies the requirements of the particular exemption statute. Whether an organization has satisfied the operational test is a question of fact.

In Old Dominion Box Co. v. United States, 477 F.2d 344 (4<sup>th</sup> Cir. 1973), Cert. Denied 413 U.S. 910 (1973), the court held that operating for the benefit of private parties constitutes a substantial non-exempt purpose.

In Stevens Bros. Foundation, Inc. v. Commissioner, 324 F.2d 633 (10<sup>th</sup> Cir. 1963), affirming 39 T.C. 93 (1962), an organization's exemption was revoked for failure to operate exclusively for charitable purposes where it entered into a partnership with and advanced funds to a for-profit entity owned and controlled by the organization's directors. The for-profit entity needed the funds to obtain construction contracts, which ultimately proved profitable. The court reasoned that the organization engaged in the transactions substantially for the purpose of benefiting its founders.

In P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), a nonprofit organization's regularly scheduled bingo games were held on the premises of a for-profit business which sold food and beverages, the games were conducted by the owners of the for-profit, and the directors of the for-profit controlled the non-profit's board. Under these circumstances, the court held that the nonprofit had a substantial non-exempt purpose to enhance the profits of the for-profit.

Rev. Proc. 2001-4, 2001-1 I.R.B. 239 sets forth general procedures for the issuance of rulings on issues under the jurisdiction of the Office of the Commissioner, Tax Exempt and Government Entities Division.

Section 8.01 of Rev. Proc. 2000-4, supra, provides that the Service ordinarily will not issue a letter ruling or determination letter in certain cases because of the factual nature of the problem involved or because of other reasons. The Service may decline to issue a letter ruling or a determination letter when appropriate in the interest of sound tax administration or on other grounds whenever warranted by the facts and circumstances of a particular case. If an applicant does not supply the information needed or fails to furnish a sufficiently detailed description of its proposed activities to permit a conclusion that it will clearly be exempt, a record of actual operations may be required before a ruling or determination letter can be issued.

Section 5 of Rev. Proc. 90-27, 1990-1 C.B. 514, provides that where an organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt a record of actual operations may be required before a ruling or determination letter can be issued.

Whether an organization has satisfied the operational test is a question of fact. See Harding Hospital, Inc. v. United States, supra. In addition, the existence of more than an insubstantial nonexempt purpose will preclude exemption. See Better Business Bureau of Washington, D.C., Inc. v. United States, supra. See also Old Dominion Box Co. v. United States, supra, which holds that operating for the private benefit of individuals is a substantial nonexempt purpose. As emphasized by the Supreme Court in United States v. Wells Fargo Bank, supra, qualification must be proven unambiguously.

The information you have submitted establishes that you are still in your infancy and have carried on at least six continuing professional educational programs over the last two years. The amount of time you have expended on your continuing professional education classes you have offered is approximately [REDACTED] hours over the last two years and the expenses incurred are approximately \$ [REDACTED]. Although you anticipate engaging in a broad teleconferencing program and will be heavily involved in continuing education programs with an emphasis on videoconferencing, your activities in this regard to date have been minimal. You have not been able to establish your proposed program of providing videoconferencing capabilities to the region. In fact you have represented that the University with which you expect to be working has not yet established the infrastructure to support a videoconferencing program. Without these activities in place, we are unable to conclude either that these activities will be operated in a charitable manner and the size of your proposed charitable program.

Nor can we compare the proper extent of your educational or charitable activities to the extent [REDACTED] has benefited by reason of your operations. The information submitted establishes that your equipment is being leased to a private dental practice, [REDACTED]. The use by [REDACTED] appears to account for the bulk of the time your computers are in use. You have even purchased or obtained business programs which appear to be used only by [REDACTED]. Your equipment is currently located in two of [REDACTED]'s dental offices and it appears that you are seeking a grant to provide funding to place equipment in their third business office. In this latest grant request you have specifically included a request for the business software needed by [REDACTED] for its billings and business management, even though you indicate that your only need for this software is to enable [REDACTED] carry out its own business on your computers. You have represented that the entire lease arrangement with [REDACTED] is reasonable and have submitted a letter from an accounting firm to that effect. However, we note that the letter from the accounting firm indicates that they were merely considering the rent of the equipment per se and do not apparently take into account the fact that the dental practice is apparently getting all of its billing and accounting services provided through use of these computers. The financial information submitted establishes that the fees paid under the lease only slightly exceed the monies needed to retire the debt you incurred in purchasing and installing the equipment. We also note that because two of the principals

of [REDACTED] are on your board of directors and participated in controlling your affairs and the other two have a working relationship with [REDACTED] there is little information available to lead to the conclusion that this lease arrangement was entered into at arms length. Operating in a manner which benefits a private party to more than an insubstantial degree may preclude exemption. Because we are unable to compare your educational program to the benefit [REDACTED] receives by reason of its lease of your equipment, we are unable to conclude that this benefit is less than insubstantial.

We recognize that the employees of [REDACTED] and its officers are involved in providing volunteer services to you and help you accomplish your exempt educational purposes. However, this does not outweigh the substantial benefit [REDACTED] receives by reason of their virtually unlimited access to your equipment. Accordingly, it appears that you have a substantial nonexempt purpose to benefit [REDACTED]. See Old Dominion Box Co. v. United States, *supra*, which holds that operating for the private benefit of individuals is a substantial nonexempt purpose.

Again, we wish to emphasize that two of the members of your board are principals of [REDACTED] and the other two share office space owned by [REDACTED] and at one time considered leasing your computer equipment. The Courts have often denied exemption where a small group of individuals control a nonprofit organization and use it for their own for-profit enterprise. See for example Stevens Bros. Foundation, Inc. v. Commissioner, *supra*, where an exempt organization invested in a for profit owned by its directors and P.L.L. Scholarship Fund v. Commissioner, *supra* where a nonprofit organization's regularly scheduled bingo games were held on the premises of a for-profit business, which was established and controlled by the for profit's board. Here again [REDACTED] use of the commuter equipment needed to carry on your educational program and the current size of your educational program strongly indicate that you are operating for the private benefit of [REDACTED].

Accordingly, we have concluded that you have not established that you qualify for recognition of exemption under section 501(c)(3) of the Code. Contributions to you are not deductible under section 170 and you are required to file Federal income tax returns.

In this proposed adverse determination we have not made a determination as to whether you would qualify as a publicly supported organization described in either section 509(a)(1) and 170(b)(1)(A)(vi) or 509(a)(2) of the Code. However, we have noted that a large amount of your income regularly comes through your lease with RGMOS and these monies have nothing to do with the accomplishment of your exempt purposes. Where an organization receives substantially all of its income from an activity unrelated to the accomplishment of its exempt purposes it could be classified as a private foundation as that term is described in section 509(a). Under the particular facts of this situation classification as a private foundation could preclude your ability to operate.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your principal officers, must be submitted within 30 days from the date of this letter. You also have the right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your principal officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practice Procedures.

[REDACTED]

If you do not protest this proposed ruling in a timely manner, it will be considered by the Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the United States Tax Court, the U.S. Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

Sincerely yours,

TSI

Terrell M. Berkovsky  
Manager, Exempt Organizations  
Technical Group 2

cc: [REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]

[REDACTED] [REDACTED]